

This review sheet is intended to cover everything that could be on the exam; however, it is possible that I will have accidentally left something off. You are still responsible for everything in the chapters covered except anything that I explicitly say you are not responsible for. Therefore, if I left something off of this sheet, it can still be on the exam. There will be no multiple-choice questions. Most of the questions will be like the ones in the homework assignments, and possibly a few definition questions, but I am more likely to ask questions that make you use the definitions rather than recite them. I will probably ask one of the questions from the book at the end of the chapters.

The review session will be at a time to be determined in class, probably Sunday 4/6 in the normal room.

Chapter 8: Skip the material from Exam #2. Start with knowing how to get from GDP to NDP, NI, PI, and DPI. Note that if you know what those terms are trying to measure, you ought to be able to figure out what is added and what is subtracted. Capital consumption allowance is another way to calculate depreciation. What is the difference between real and nominal GDP? Ignore the chain-weighted measure for real GDP. How do we compare GDP across countries?

Chapter 9: What is economic growth? What are the negative effects of economic growth? What is the problem of using this as a measure of welfare? What causes GDP per capita to grow? Why do small changes in the growth of GDP matter? What is labor productivity and what changes it? Why is saving so important to growth? What is human capital? What are the advantages and disadvantages of patents? Why do open economies grow faster? How does population growth affect development? Why are property rights important for growth? The four keys to development on page 231 will help you to understand parts of the chapter.

Chapter 10: What is meant by the term *long-run aggregate supply curve*? What determines its shape and its location? How does it relate to the PPF, a.k.a. the PPC? What is aggregate demand? Why does it take its shape? **Note the logic used for the demand curve's slope does not apply to the slope of the aggregate demand curve.** What moves the AD curve? (Anything that changes the demand for goods and/or services, other than price induced changes in the demand, will move AD.) Remember that for all curves, if a variable on one axis changes causing the other variable to change, then you did not move the curve, you retraced it. What causes inflation? What are demand pull and cost push inflation? The book goes into more detail in Chapter 11.

Chapter 11: What are the four assumptions of the classical school? What did Say say? How does it relate to the SRAS curve? Note that we went into more detail than the book on that explanation. How does it relate to labor supply and labor demand? Why should  $S = I$ ? What assumptions did Keynes make? How did that relate to the SRAS curve? Why do we draw the "Modern" SRAS? Unless I specify otherwise, when I refer to the SRAS, use the "Modern SRAS." What moves the SRAS? Notice that the only thing that moves SRAS without moving LRAS is the price of inputs because they do not affect how much could be produced if we are at full employment. Note the book has useful tables on pages 247 (Chapter 10) and 274, which is slightly misleading in the next to last line. Marginal **business and/or sales** tax rates move the SRAS because it is a cost of production, while marginal **income** tax rates affect aggregate demand because they reduce income, not raising the cost of production. The prices of inputs only temporarily affect the costs of production without any long-term effects. Since expected future price increases will increase wages, which are an input price, it will move only the AD and SRAS curves but not the LRAS curve. What is meant by *supply shock* and *demand shock*? What are inflationary and recessionary gaps? How will they solve themselves if the government takes no actions? What are the demand pull and cost push inflations? How does a change in the value of the dollar on the foreign exchange market affect the SRAS/LRAS/AD diagram? Note that the book should combine the panels in figure 11-14. Unless specified otherwise, use the "modern" SRAS curve when asked for the SRAS curve. If you are not told that unemployment is high or low (recessionary gap or inflationary gap respectively), start your graph with LRAS crossing SRAS where it crosses AD.

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This is the non-graded Assignment #6A that will be reviewed with Assignment #6.

- 1) (10 points) Draw the "Modern AD" curve. Explain why it takes its shape.
- 2) (20 points each) Illustrate the following events on the SRAS/LRAS/AD diagram. Explain why the curve(s) moved as drawn. What happens to the price level and GDP? (All of these are occurring as you do this question.)
  - A) The government spends more.
  - B) Oil prices go up.
  - C) Consumers get fearful about the future, so they decide to save more.
  - D) The dollar loses value on the foreign exchange market.
- 3) (10 points) What moves the LRAS curve? Why does that move the curve?